



OFFICE OF MAYOR JERRY SANDERS

FOR IMMEDIATE RELEASE

March 14, 2006

FACT SHEET

SUNSHINE WEEK

SANDERS ANNOUNCES \$1 BILLION RETIREE MEDICAL LIABILITY; LIABILITY GROWS TO \$1.8 BILLION IN 9 YEARS

**SAN DIEGO AMONG THE FIRST GOVERNMENT AGENCIES NATIONWIDE TO ANNOUNCE
LIABILITY; CITY WILL NOT BE ALONE IN LARGE NUMBERS; ACCOUNTING STANDARDS
PROMPT GOVERNMENT AGENCIES TO BOOK LIABILITY BY FY08**

MAYOR'S BUDGET WILL INCLUDE "PAY AS YOU GO" CONTRIBUTION IN FY07 BUDGET

Background:

- In accordance with the Government Accounting Standards Board (GASB) Statement 45 ("Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions"), government entities will have to begin booking the liability of their unfunded healthcare benefits ("Net Other Post Employment Benefit (OPEB) Obligation") on their financial statements.
- As of FY08, valuation studies like this one will be mandatory for any government entity that offers healthcare benefits to retirees.
- In 2005, the City commissioned Towers Perrin to perform a valuation of the post-retirement health care benefits offered to City retirees. Their report is being released today.
- This report was commissioned for the purpose of determining the City's annual cost of retiree health care costs. **The City of San Diego is one of the first cities in the nation to have performed this valuation study.**

Definitions:

Normal Cost: The value of an active employee's retiree health care benefit that is assigned to one year of service. (See page 3, 19 and 20: Normal Cost for FY06 would be \$46.1 million.)

Actuarial Accrued Liability (AAL): The liability for the health care benefits of those City employees who have already retired plus the value of retiree medical benefits of active employees assigned to service already rendered. This number will grow over time. (See page 2: **while the AAL is \$978 million in FY06, it grows to \$1.9 billion over the next 9 years.**)

Unfunded AAL (UAAL): Whatever portion of the AAL the City has not funded into an irrevocable trust. For instance, on Page 19 (top chart), if the City makes no contribution toward the AAL, the UAAL remains the same. Whereas on the bottom chart, if the City makes a contribution toward the AAL, the UAAL goes down.

Amortization, 15/30 Year: The amount that would have to be paid annually, depending on the amortization, to pay off a portion of the AAL (See page 3: the 30 year amortization is \$69 million.)

Annual Required Contribution (ARC): The contribution thought to be necessary on an annual basis to fully fund the health care benefits of both active and retired employees. For FY06, this amount would be \$115 million. The ARC is arrived at by adding the following two numbers:

Normal Costs:	\$46,087,689
<u>Rolling Amortization/UAAL:</u>	<u>\$69,033,097</u>
Annual Required Contribution:	\$115,120,786

For this group of employees only: the \$115 million represents 17.7% of the City's payroll. Pension benefits costs are thought to constitute an additional 26% of payroll. As a result, the City's pension and healthcare benefits costs aggregate to 44% of payroll.

Benefits Disbursement or "Pay as You Go": The practice of only paying for the benefits of retirees as those expenses become due. It is thought that 90% of cities nationwide use this financing method.

<p><i>MAYOR'S FY07 BUDGET WILL INCLUDE "PAY AS YOU GO"</i></p> <p><i>CONTRIBUTION OF APPROXIMATELY \$21 MILLION</i></p>

Study Assumptions

- Both 15 and 30 year amortization schedules were prepared (page 19 and page 20). The actuarial accrued liability is the same for both schedules; what varies is the Annual Required Contribution.

- For this study, there were 10,426 active employees eligible for postretirement health care benefits and 4,159 retirees receiving those benefits.

Applicable City Policies

- Retiree healthcare benefits will no longer be offered to City employees hired after July 1, 2005. The system is therefore considered a “closed system.”
- For employees hired prior to July 1, 2005, City-subsidized healthcare is offered to the employee only at retirement -- not their spouse or family, although they can purchase the healthcare for them at group rates.
- Retired employees are offered an annual benefit of \$7,225 toward healthcare (the equivalent of the cost of a PPO plan for a single individual). If they purchase a healthcare plan that does not cost that much, they are not able to use the remaining funds.
- In 1982, City employees voted to get out of the Social Security/Medicare systems. In exchange, they were promised life-time health insurance upon retirement.
- Beginning on April 1, 1986, the Federal government required that all employers and employees pay into Medicare going forward. Since that time, the City pays into Medicare for employees hired after that date.
- The impact of purchase of service credits on the cost of retiree health care benefits was not part of this valuation study. It will be a part of an updated study.

Current (FY06) Healthcare/Flex Benefit Costs for Active City Employees:

Employee Healthcare Only	\$40,399,175
Employee + Dependents Healthcare	\$47,716,755
All Flexible Benefits (includes dental, vision, other benefits)	\$60,078,275

Potential Scenarios:

1. Pay the ARC + Current Healthcare Costs for Active City Employees (FY06: \$156 million)
2. Continue “Pay as You Go” + Current Healthcare Costs for Active City Employees (FY06: \$57 million)

3. Middle ground with negotiation of benefits level that retirees receive

City of San Diego
Retiree Medical Benefit Plan

Actuarial Valuation Report

**Retiree Medical Benefit Plan Liabilities as of June 30, 2005 to
Develop the Cost for Fiscal Year Ending June 30, 2006**

March 2006

This report is confidential and intended solely for the information and benefit of the immediate recipient thereof. It may not be distributed to a third party unless expressly allowed under the "Actuarial Certification, Reliances and Distribution" section herein.

Supplemental Information

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Appendices

Documentation of Assumptions and Methods

Estimated Projection of Retiree Medical Benefit Plan Valuation Results

Actuarial Certification, Reliances and Distribution

The City of San Diego retained Towers Perrin to perform a valuation of its postretirement welfare benefit plans for the purpose of determining its annual cost in accordance with GASB Statement No. 45 – *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This valuation has been conducted in accordance with generally accepted actuarial principles and practices.

The consulting actuary is a member of the Society of Actuaries and other professional actuarial organizations and meets their “General Qualification Standard for Public Statements of Actuarial Opinion” relating to postretirement welfare plans.

In preparing the results presented in this report, we have relied upon information provided to us regarding plan provisions, plan participants, and plan assets. We have reviewed this information for overall reasonableness and consistency, but have neither audited nor independently verified this information. The accuracy of the results presented in this report is dependent upon the accuracy and completeness of the underlying information.

The actuarial assumptions and the accounting policies and methods (except for the discount rate and the Entry Age Normal cost method) employed in the development of the postretirement welfare cost have been selected by Towers Perrin, which relied upon actuarial audits and experience studies conducted for SDCERS. We did not independently study historic information to develop assumptions. The amortization of unfunded liabilities as a level dollar amount over 30 years was selected by Towers Perrin to comply with GASB 45 requirements for a plan closed to new entrants. At the request of the City, we also prepared valuation results using a 15-year amortization period, shown in the appendix in the form of a ten-year projection. The City selected the discount rate based on an expected return on assets for a pre-funded plan. The City also requested that the Entry Age Normal cost method be used. When the benefit is prefunded with an irrevocable trust, a method for valuing assets (e.g., market value or a smooth approach) will need to be selected. Next year when the second valuation is completed, the City will need to decide if a 30-year amortization period will again be used (rolling) or if the amortization period will decrease by a year (declining).

The results shown in this report have been developed on the basis of actuarial assumptions that are considered to be reasonable and within the “best-estimate range” as described by the Actuarial Standards of Practice. Other actuarial assumptions could also be considered to be reasonable and within the best-estimate range. Thus, reasonable results differing from those presented in this report could have been developed by selecting different points within the best-estimate ranges for various assumptions.

The information contained in this report was prepared for the internal use of the City of San Diego and its auditors in connection with the actuarial valuation of the postretirement welfare plan. It is neither intended nor necessarily suitable for other purposes. The City of San Diego may also distribute this actuarial valuation report to parties who have a legal right to require the City to provide them with this report, in which case the City of San Diego will provide this report in its entirety including all assumptions, caveats and limitations.

Leslie P. Finertie

Leslie P. Finertie, F.S.A., E.A., M.A.A.A., F.C.A.
Towers Perrin
March 2006

Basic Estimated Results for Postretirement Welfare Cost

June 30, 2005

	Safety	General	Total
Normal Cost			
Medical	\$ 13,732,585	\$ 23,861,897	\$ 37,594,482
Medicare Supplement	<u>2,001,718</u>	<u>5,168,122</u>	<u>7,169,840</u>
Total	\$ 15,734,303	\$ 29,030,019	\$ 44,764,322

Actuarial Accrued Liability (AAL)

Medical:

▶ Retirees	\$ 144,488,825	\$ 138,946,302	\$ 283,435,127
▶ DROP participants	35,102,402	35,411,933	70,514,335
▶ Vested terminations	1,639,286	6,424,266	8,063,552
▶ Actives	<u>150,765,447</u>	<u>312,241,949</u>	<u>463,007,396</u>
Total Medical	\$ 331,995,960	\$ 493,024,450	\$ 825,020,410

Medicare Supplement:

▶ Retirees	\$ 17,264,572	\$ 29,697,628	\$ 46,962,200
▶ DROP participants	6,194,533	8,082,328	14,276,861
▶ Vested terminations	327,857	1,284,853	1,612,710
▶ Actives	<u>24,673,068</u>	<u>65,775,303</u>	<u>90,448,371</u>
Total Medical	\$ 48,460,030	\$ 104,840,112	\$ 153,300,142

Total AAL:

▶ Retirees	\$ 161,753,397	\$ 168,643,930	\$ 330,397,327
▶ DROP participants	41,296,935	43,494,261	84,791,196
▶ Vested terminations	1,967,143	7,709,119	9,676,262
▶ Actives	<u>175,438,515</u>	<u>378,017,252</u>	<u>553,455,767</u>
Total AAL	\$ 380,455,990	\$ 597,864,5629	\$ 978,3207,552

Estimated Annual Required Contribution

	Fiscal Year 2006		
	Safety	General	Total
Normal Cost			
▶ Beginning of Year	\$ 15,734,303	\$ 29,030,019	\$ 44,764,322
▶ Adjusted to Mid-Year	16,199,456	29,888,233	46,087,689
▶ Percent of Payroll	6.94%	7.17%	7.09%
Funded Status			
▶ Actuarial Accrued Liability (AAL)	\$ 380,455,990	\$ 597,864,562	\$ 978,320,552
▶ Value of Plan Assets	0	0	0
▶ Unfunded Actuarial Accrued Liability (UAAL)	\$ 380,455,990	\$ 597,864,562	\$ 978,320,552
UAAL Amortization			
▶ Amortization Method	Level Dollar	Level Dollar	Level Dollar
▶ Amortization Period	30 Years	30 Years	30 Years
▶ Amortization of UAAL	\$ 26,846,063	\$ 42,187,034	\$ 69,033,097
▶ Percent of Payroll	11.49%	10.12%	10.62%
Annual Required Contribution (ARC)			
▶ Percent Payroll	18.43%	17.29%	17.70%
Actuarial Cost Method			
	Entry Age Normal	Entry Age Normal	Entry Age Normal
Actuarial Assumptions			
▶ Investment Rate of Return	6.00%	6.00%	6.00%
▶ Projected Salary Increases	3.00%	3.00%	3.00%
Valuation Payroll			
▶ Beginning of Year	\$ 230,145,730	\$ 410,642,864	\$ 640,788,594
▶ Adjusted to Mid-Year	233,572,406	416,756,990	650,329,396

Actuarial Assumptions and Methods

Please see the appendices for additional background on the assumptions and methods.

Economic Assumptions

Discount rate	6.00%
Inflation portion of salary increase rate	3.00%

Medical Benefit Assumptions

Medical plan premium trend rate:	10% reducing 0.5% per year reaching an ultimate rate of 5.5%
City medical premium reimbursement cap trend rate:	Based on CMS projected trends at an initial rate of 7.3% and decreasing to 5.5% in 2014 and thereafter

From	To	Increase
2004	2005	7.3%
2005	2006	7.3%
2006	2007	7.5%
2007	2008	7.5%
2008	2009	7.3%
2009	2010	7.0%
2010	2011	6.9%
2011	2012	6.9%
2012	2013	6.8%
2013	2014	6.7%
2014 and thereafter		5.5%

Future medical plan election	Active, DROP and vested terminated members who are not currently enrolled in retiree medical coverage are assumed to elect the various medical plan coverages in the same proportion as current retiree elections.
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Administrative expenses	None considered other than those included in the premiums charged to members or paid for by the City.
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MMA Assumptions

No explicit assumption because the City's obligation is to reimburse medical plan premiums and Medicare Part B up to an annual limit. Any reductions due to Medicare Part D subsidies will be reflected in future premiums charged to retirees.

Medicare Part B

Reimbursement Assumptions

Future Medicare eligibility	100% assumed for those hired on or after April 1, 1986, with 80% assumed eligible for actives hired prior to April 1, 1986. For retired participants currently under age 65, 60% are assumed to become eligible for Medicare Part B.
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Reimbursement per participant \$78.20 per month in 2005 increasing to \$88.10 as of January 1, 2006. Thereafter, the average reimbursement for 2005–2006 is projected by the Medicare Part B trend rate.

Medicare Part B trend rate Same as the medical plan premium trend rate.

Demographic and Other Assumptions

Mortality:

- ▶ Healthy RP2000 Combined Healthy Mortality Table projected to 2015 (male and female)
- ▶ Disabled RP2000 Combined Healthy Mortality Table projected to 2015 (male and female)

Termination Rates varying by age and service. Sample rates are shown below:

<u>Age</u>	<u>Years of Service</u>	<u>Safety</u>	<u>General</u>
All	0	3.0%	7.0%
	1	2.0	6.0
	2	2.0	4.3
	3	2.0	4.3
	4	2.0	4.2
20	5+	2.4	4.6
25		2.3	4.6
30		1.9	3.8
35		1.2	2.5
40		0.6	2.0
45		0.4	1.6
50		0.1	1.4
55		0.0	1.2

Disablement

Varies by age. Sample rates are shown below:

<u>Age</u>	<u>Safety</u>	<u>General</u>
20	0.54%	0.06%
25	0.60	0.08
30	0.65	0.10
35	0.71	0.16
40	0.90	0.22
45	1.15	0.33
50	1.25	0.50
55	1.50	0.75

70% of General disabilities and 85% of Safety disabilities are assumed to be "duty-disability."

Retirement

Varies by age.

<u>Age</u>	<u>Safety</u>	<u>General</u>
50	30.0%	0.0%
51	20.0	0.0
52	20.0	0.0
53	30.0	0.0
54	30.0	0.0
55	50.0	20.0
56	40.0	10.0
57	40.0	10.0
58	40.0	15.0
59	60.0	15.0
60	75.0	20.0
61	80.0	25.0
62	100.0	50.0
63	100.0	40.0
64	100.0	25.0
65	100.0	50.0
66	100.0	40.0
67	100.0	40.0
68	100.0	40.0
69	100.0	40.0
70	100.0	100.0

For all members, 100.0% are assumed to retire at the later of age 55 and 30 years of service. 50% of active members expected to retire in the future are assumed to defer pre-65 retiree medical benefits for two years because of enrollment in the DROP. However, their post-65 medical benefits are assumed to commence at age 65. Current vested terminated participants are assumed to retire as soon as eligible and current DROP participants are assumed to retire in one year

Percent married

N/A, no dependent coverage.

Participation

Future retirees are expected to select the same medical plans as current retirees, with 86% selecting some coverage in addition to Medicare.

Cash flows for postretirement welfare cost purposes:

- ▶ Amount and timing of contributions
- ▶ Timing of benefit payments

Contributions are made midyear.

Benefit payments are assumed to be made uniformly throughout the year and on average at midyear.

Methods

Measurement date	Fiscal year-end.
Service cost and AAL	Entry Age Normal actuarial cost method, allocated in equal amounts, from the valuation date on or after date of hire to full eligibility date.
Amortization of UAAL	Level dollar amount
Asset valuation	Not currently applicable.

Benefits Not Valued

All benefits described in the Plan Provisions section were valued except that medical claims reimbursable to retirees electing private coverage were not considered. Data should be collected in the future to estimate this liability for these participants, currently representing less than 5% of retirees. Towers Perrin has reviewed the plan provisions with the City and based on that review is not aware of any other significant benefits required to be valued that were not.

Data Sources

The City of San Diego furnished participant data and premium rates as of June 30, 2005. Data were reviewed for reasonableness and consistency, but no audit was performed. Assumptions or estimates were made by Towers Perrin based on input from the City when data were not available. We are not aware of any errors or omissions in the data that would have a significant effect on the results of our calculations.

Participant Data

Summary of Participant Data as of June 30, 2005

	Number of Members	Average Age	Average Service
▶ Active Members (Excluding DROP Participants):			
– Safety	2,614	39.8	13.0
– General	<u>6,850</u>	<u>44.1</u>	<u>12.2</u>
– Total	9,464	42.9	12.4
▶ DROP Participants:			
– Safety	386	54.8	27.7
– General	<u>493</u>	<u>59.8</u>	<u>25.0</u>
– Total	879	57.6	26.2
▶ Vested Terminated Participants:			
– Safety	19	43.0	17.6
– General	<u>64</u>	<u>49.6</u>	<u>17.4</u>
– Total	83	48.1	17.4
▶ Retirees (including those waiving coverage and those not eligible for coverage):			
– Safety	1,734	63.3	N/A
– General	<u>2,425</u>	<u>69.3</u>	N/A
– Total	4,159	66.8	N/A

Summary of Retiree Data

	By Health Benefits Status		
	Eligible for Health Benefits	Not Eligible for Health Benefits	Expected to Receive Medicare Part B
Participants whose current age is:			
Under 65	1,640	122	1,245
Over 65	<u>1,493</u>	<u>473</u>	<u>1,503</u>
Total	3,133	595	2,748
Not Participants	431	-	1,411
Total Retirees	3,564	595	4,159

2005 — 2006 Potential Retiree Monthly Premium Reimbursement

Provider	Not Medicare Eligible	Medicare Eligible
Kaiser/Senior Advantage	\$ 466.74	\$ 253.50
Kaiser Colorado	467.78	147.33
Kaiser Georgia	619.72	259.42
Kaiser Hawaii	446.49	218.95
Kaiser Northwest	496.06	169.95
Local 127 PacifiCare HMO	323.57	323.57
MEA Sharp HMO	288.00	288.00
POA Healthnet HMO	316.73	316.73
PacifiCare HMO/Secure Horizons	518.12	193.98
PacifiCare PPO	643.61	193.98
PacifiCare HMO/Secure Horizons	518.12	193.98
Kaiser/Senior Advantage	466.74	253.50
Senior Supplement	643.61	439.77
Private (Average)	226.71	110.35
Local 145 Healthnet HMO	402.57	268.72
Local 145 Healthnet PPO	692.35	594.08
POA Healthnet PPO	748.67	449.37
Medicare Part B	N/A	78.20/88.10

Note: Above premiums may be reimbursed by the City up to a dollar cap. Reimbursement for claims of retirees taking private coverage was not considered in this valuation.

City of San Diego Participant Data for Active and DROP Members as of June 30, 2005

Age Nearest Birthday	Completed Years of Service							Total
	0 to 4	5 to 9	10 to 14	15 to 19	20 to 24	25 to 29	30 to 34	Over 34
15 to 19	2	0	0	0	0	0	0	-
20 to 24	113	16	0	0	0	0	0	-
25 to 29	403	188	21	0	0	0	0	-
30 to 34	372	433	156	22	0	0	0	-
35 to 39	304	483	413	288	22	0	0	-
40 to 44	226	389	373	704	279	21	1	-
45 to 49	170	277	282	571	425	241	16	-
50 to 54	146	186	220	341	278	309	183	26
55 to 59	63	122	113	183	130	136	185	67
60 to 64	32	41	54	82	45	21	40	27
65 to 69	4	14	12	22	9	9	5	1
Over 69	-	3	6	5	4	1	4	3
Total	1,835	2,152	1,650	2,218	1,192	738	434	124
								10,343



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Summary of Participant Data by Provider

Provider	Active Members*	Vested Terminated Members	Retirees
Kaiser/Senior Advantage	1,664	13	610
Kaiser Colorado	13	0	4
Kaiser Georgia	22	0	9
Kaiser Hawaii	19	0	8
Kaiser Maryland*	0	0	1
Kaiser Northwest	32	1	13
Local 127 Pacificare	128	1	48
MEA Sharp HMO	361	2	135
POA Healthnet HMO	476	4	168
PacifiCare COB*	0	0	34
PacifiCare HMO/Secure Horizons	757	6	284
PacifiCare PPO	545	5	200
PacifiCare HMO/Secure Horizons	663	5	224
Kaiser/Senior Advantage	1,726	14	596
Senior Supplement	590	5	228
Private	886	6	185
Local 145 Healthnet HMO	211	2	72
Local 145 Healthnet PPO	597	5	206
POA Healthnet PPO	238	2	88
Kaiser M**	0	0	3
Medicare Only	754	6	282
No Plan	661	6	111
\$100 per Month	0	0	650
Total	10,343	83	4,159

* Allocated based on current retiree elections rather than current active coverage.

** Discontinued plans

Plan Provisions

The following summary of plan provisions represents our understanding of the substantive plan.

Medical Benefits

Eligibility	<p>The plan provides benefits to Medical Health eligible retirees and Non-Health Eligible retirees who were hired by the City prior to July 1, 2005. Those employees hired on or after July 1, 2005 are not eligible for this plan.</p> <p>Health Eligible retirees are those who:</p> <ul style="list-style-type: none"> ▶ Were hired on or before June 30, 2005; ▶ Are eligible for and receive a retirement allowance from SDCERS; ▶ Were on the active payroll of the City of San Diego on or after October 5, 1980; and ▶ Retired on or after October 6, 1980 from the City of San Diego. <p>Non-Health Eligible retirees are those who:</p> <ul style="list-style-type: none"> ▶ Are eligible for and receive a retirement allowance from SDCERS; and ▶ Retired before October 6, 1980, from City of San Diego employment. <p>Retirement allowances are granted to service, vested termination and disability retirements.</p>
Retirement Date	<ul style="list-style-type: none"> ▶ General: Age 62 with ten years of service or age 55 with 20 years of service. ▶ Safety: Age 55 with ten years of service or age 50 with 20 years of service.
Service retirements	Employees who retire from active status on or after the Retirement Date can immediately commence medical benefits.
Vested terminated retirements	Employees who complete ten years of service at termination can immediately commence medical benefits at the Retirement Date.
Disability retirements	<p>Employees who become disabled due to duty-related disability can immediately commence medical benefits.</p> <p>Employees who completed ten years of service and become disabled due to non-duty-related disability can immediately commence medical benefits.</p>
Dependent eligibility	None.
Survivor eligibility	None.

Benefits**Health Eligible Retirees:**

- ▶ Non-Medicare eligible retirees receive reimbursements of actual HMO or PPO premium, up to \$602.04 per month for the fiscal year beginning July 1, 2005
- ▶ Medicare eligible retirees receive reimbursements of actual HMO or PPO premium, up to \$566.98 per month for the fiscal year beginning July 1, 2005
- ▶ Medicare eligible retirees also receive reimbursements of Medicare Part B premium, which is \$88.10 per month effective January 1, 2006
- ▶ The maximum reimbursement levels are increased each year by the projected percentage increase in the total National Health Expenditures as stated by CMS for that year.

Non-Health Eligible Retirees:

- ▶ Reimbursed up to \$100 per month for incurred medical expenses and Medicare Part B premium. The maximum reimbursement level does not increase.

**Other Postretirement
Welfare Benefits**

None.

Glossary

Actuarial assumptions. Assumptions as to the occurrence of future events affecting retirement costs, such as: mortality, withdrawal, disablement and retirement, changes in compensation and investment earnings.

Actuarial accrued liability. That portion, as determined by a particular Actuarial Cost Method, of the Actuarial Present Value of retirement plan benefits and expenses, which is not provided for by future Normal Costs.

Actuarial cost method or funding method. A procedure for determining the Actuarial Present Value of retirement plan benefits and expenses and for developing an actuarially equivalent allocation of such value to time periods, usually in the form of a Normal Cost and an Actuarial Accrued Liability.

Actuarial gain (loss) or experience gain (loss). A measure of the difference between actual experience and that expected based upon a set of Actuarial Assumptions, during the period between two Actuarial Valuation dates, as determined in accordance with a particular Actuarial Cost Method.

Actuarial present value of total projected benefits. Total projected benefits include all benefits estimated to be payable to plan members (retirees and beneficiaries, terminated employees entitled to benefits but not yet receiving them, and current active members) as a result of their service through the valuation date and their expected future service. The actuarial present value of total projected benefits as of the valuation date is the present value of the cost to finance benefits payable in the future, discounted to reflect the expected effects of the time value (present value) of money and the probabilities of payment.

Actuarial valuation. The determination, as of a valuation date, of the Normal Cost, Actuarial Accrued Liability, Actuarial Value of Assets, and related Actuarial Present Values for a retirement plan.

Actuarial value of assets or valuation assets. The value of cash, investments and other property belonging to a retirement plan, as used by the actuary for the purpose of an Actuarial Valuation.

Amortization payment. That portion of the retirement plan contribution, which is designed to pay interest on and to amortize the Unfunded Actuarial Accrued Liability.

Annual required contributions of the employer (ARC). The employer's periodic required contributions to a defined benefit OPEB plan, calculated in accordance with the parameters.

Centers for Medicare & Medicaid Services (CMS). Organization which projects increases in Medicare costs used for projecting premium caps under City of San Diego union contracts.

Defined benefit OPEB plan. An OPEB plan having terms that specify the *benefits* to be provided at or after separation from employment. The benefits may be specified in dollars (for example, a flat dollar payment or an amount based on one or more factors such as age, years of service, and compensation), or as a type or level of coverage (for example, prescription drugs or a percentage of healthcare insurance premiums).

Employer's contributions. Contributions made in relation to the annual required contributions of the employer (ARC). An employer has made a contribution in relation to the ARC if the employer has (a) made payments of benefits directly to or on behalf of a retiree or beneficiary, (b) made premium payments to an insured or (c) irrevocably transferred assets to a trust, or equivalent arrangement, in which plan assets are dedicated to providing benefits to retirees and the beneficiaries in accordance with the terms of the plan and are legally protected from creditors of the employer(s) or plan administrator.

Entry age actuarial cost method. A method under which the Actuarial Present Value of the Projected Benefits of each individual included in an Actuarial Valuation is allocated on a level basis over the earnings or service of the individual between entry age and assumed exit age(s). The portion of this Actuarial Present Value allocated to a valuation year is called the Normal Cost. The portion of this Actuarial Present Value not provided for at a valuation date by the Actuarial Present Value of future Normal Costs is called the Actuarial Accrued Liability.

Funded ratio. The actuarial value of assets expressed as a percentage of the actuarial accrued liability.

Healthcare cost trend rate. The rate of change in per capita health claims costs over time as a result of factors such as medical inflation, utilization of healthcare services, plan design, and technological developments.

Investment return assumption (discount rate). The rate used to adjust a series of future payments to reflect the time value of money.

Medicare Modernization Act (MMA). The federal law which created Medicare Part D.

Net OPEB obligation. The cumulative difference since the effective date of this statement between annual OPEB cost and the employer's contributions to the plan including the OPEB liability (asset) at transition, if any, and excluding (a) short-term differences and (b) unpaid contributions that have been converted to OPEB-related debt.

Normal cost. That portion of the Actuarial Present Value of retirement plan benefits and expenses, which is allocated to a valuation year by the Actuarial Cost Method.

Other postemployment benefits. Postemployment benefits other than retirement benefits. Other postemployment benefits (OPEB) include postemployment healthcare benefits, regardless of the type of plan that provides them, and all postemployment benefits provided separately from a retirement plan, excluding benefits defined as termination offers and benefits.

Pay-as-you-go. A method of financing a retirement plan under which the contributions to the plan are generally made at about the same time and in about the same amount as benefit payments and expenses becoming due.

Plan assets. Resources, usually in the form of stocks, bonds, and other classes of investments, that have been segregated and restricted in a trust, or equivalent arrangement, in which (a) employer contributions to the plan are irrevocable, (b) assets are dedicated to providing benefits to retirees and their beneficiaries, and (c) assets are legally projected from creditors of the employers or plan administrator, for the payment of benefits in accordance with the terms of the plan.

Plan members. The individuals covered by the terms of an OPEB plan. The plan membership generally includes employees in active service, terminated employees who have accumulated benefits but are not yet receiving them and retired employees and beneficiaries currently receiving benefits.

Postretirement benefit increase. An increase in the benefits of retirees or beneficiaries granted to compensate for the effects of inflation (cost-of-living adjustment) or for other reasons.

Substantive plan. The terms of an OPEB plan as understood by the employer(s) and plan members.

Unfunded actuarial accrued liability. The excess of the Actuarial Accrued Liability over the Actuarial Value of Assets.

Documentation of Assumptions and Methods for the Retiree Medical Benefit Plan Valuation

Towers Perrin considered historic information that had been developed for SDCERS, including experience studies and actuarial audits. Gabriel, Roeder, Smith & Company (GRS) conducted an experience study in 2001 and 2004. Mercer Human Resources consulting (Mercer) received GRS's work including the SDCERS actuarial assumptions and 2001 experience study in 2004. While the methodology for conducting the experience studies appears reasonable, Towers Perrin did not have historic data to audit the results. We have chosen these assumptions to be as realistic as possible to appropriately anticipate the City's reimbursement for retiree medical premiums based on the plan design and participant population at this point in time.

Economic Assumptions

The 6.0% discount rate was selected by the City. If there is not an irrevocable trust established to pay benefits, GASB 43/45 requires that the employer's expected return on its own invested assets be used to determine the discount rate. If there is an irrevocable trust to which the Annual Required Contribution (ARC) is deposited, then the expected return based on the asset mix would be considered. If over time, less than the ARC is contributed, then a pro-rata investment return based on both employer assets and trust assets would be used. GASB 43/45 is not yet effective and decisions regarding pre-funding in an irrevocable trust have not been made at this time.

The 3.0% inflation portion of the salary increase rate was selected based on the payroll growth assumption that the City had asked Towers Perrin to use for projection of pension contributions. This assumption is only used to project the payroll to develop the ARC as a percent of payroll.

Medical Benefit Assumptions

The medical plan premium trend rate starting at 10% and reducing to an ultimate rate of 5.5% is consistent with Towers Perrin's assumptions for other retiree medical valuations and represents a reasonably realistic expectation for this hard-to-predict assumption.

The City Medical premium reimbursement cap trend rate is based on CMS projections, which we understand is the negotiated index, decreasing to the ultimate trend rate of 5.5%.

The medical election for future retirees was tied to current elections made by retired employees. Because active and retiree medical plan design and premiums differ, we agreed with the City to base this assumption on elections of current retirees.

Administrative expenses are not anticipated except to the extent included in premiums. If there are significant administrative expenses to be charged to an irrevocable trust to be set up in the future, this assumption should be reconsidered.

MMA Assumptions

The valuation of post-65 benefits is based on premium reimbursement, rather than actual claims net of Medicare Part D subsidy.

Medicare Part B Reimbursement Assumptions

Future Medicare eligibility reflects that City employees hired on or after April 1, 1986 were required to pay Medicare premiums and will therefore be covered if they retire with at least ten years of employment. Others may become eligible for Medicare through other employment or a spouse. The 80% and 60% assumptions were chosen with the concurrence of the City without sufficient data to test their accuracy. As with all assumptions, these assumptions should be monitored and adjusted as appropriate going forward.

The Medicare reimbursement is based on currently known amounts through 2006 and is increased based on the same trend as the medical plan premiums thereafter.

Demographic and Other Assumptions

The RP 2000 Combined Healthy Mortality Table projected to 2015 simulates the costs of the RP 2000 generational table which was viewed as a best practice mortality table by Mercer Human Resource Consulting (Mercer) in its May 11, 2004 Audit report on actuarial issues completed for SDCERS.

The disability mortality table was selected to be the same as the healthy mortality table because longevity may not be significantly shorter for this population.

Termination was selected based on the higher rates from the Gabriel, Roeder, Smith & Company (GRS) 2004 experience investigation rather than the lower rates from the 2001 experience investigation to reflect the likelihood that current City budget constraints may result in higher turnover in the near-term future.

Disablement was selected based on the higher rates from the GRS 2001 experience investigation rather than the lower rates from the 2004 experience investigation to reflect the likelihood that current City budget constraints may result in a higher incidence of disablement in the near-term future.

Retirement rates were selected based on the GRS 2004 experience investigation which showed a higher incidence than the 2001 study. Of those actives retiring, 50% are assumed to enter a DROP period for the lesser of two years or until attainment of age 65. The 2004 GRS experience investigation shows that 75% of general and 85% of Safety "retirements" are due to DROP. The maximum period for the DROP is five years, making a two-year assumption reasonably conservative. The one-year deferred retirement assumption for those already in the DROP period is consistent with the two-year assumption for new DROP participants. The 2004 study indicated that terminated members generally retire when first eligible to do so.

Methods

The Entry Age Normal actuarial cost method was selected by the City. It is the most common method used for public sector pension funds. Typical practice for retiree medical valuations has not yet been established.

The amortization of the UAAL is a level dollar amount, consistent with GASB requirements for a closed group. The maximum amortization period allowed under GASB 43/45 is 30 years.

This is the first valuation completed for the retiree medical benefit plan of the City of San Diego. As GASB 43/45 is implemented and experience is studied, it would be appropriate to revisit these assumptions.

City of San Diego

Estimated Projection of Retiree Medical Benefit Plan Valuation Results

Projected Payroll Growth: 3.00% Annual Decrease in Active Counts: 2.50%
 Investment Rate of Return: 6.00% Amortization period: 30 years

Funding Assumption: No Pre-funding

Fiscal Year	Payroll Mid-Year	Normal Cost Mid-Year	NC as a % of Payroll	AAL	AVA	UAAAL	Amortization of UAAAL	Rolling 30-year	Annual Required Contribution	ARC as a % of Payroll	Benefit Disbursements	Employer Contributions	Net OPEB Obligation
2005	\$ 650,329,396	\$ 46,087,689	7.09%	\$ 978,320,552	\$ -	\$ 978,320,552	\$ 69,033,097	\$ 69,033,097	\$ 115,120,786	17.70%	\$ 16,772,697	\$ 16,772,697	\$101,255,555
2007	\$ 653,093,296	\$ 46,283,562	7.09%	\$ 1,067,201,417	\$ -	\$ 1,067,201,417	\$ 75,304,785	\$ 75,304,785	\$ 121,588,347	18.62%	\$ 19,638,052	\$ 19,638,052	\$204,939,035
2008	\$ 655,868,943	\$ 46,480,267	7.09%	\$ 1,158,666,734	\$ -	\$ 1,158,666,734	\$ 81,758,839	\$ 81,758,839	\$ 128,239,106	19.55%	\$ 23,060,427	\$ 23,060,427	\$310,634,857
2009	\$ 658,656,366	\$ 46,677,808	7.09%	\$ 1,252,298,939	\$ -	\$ 1,252,298,939	\$ 88,365,796	\$ 88,365,796	\$ 135,043,604	20.50%	\$ 27,108,819	\$ 27,108,819	\$417,831,327
2010	\$ 661,455,676	\$ 46,876,189	7.09%	\$ 1,347,584,382	\$ -	\$ 1,347,584,382	\$ 95,089,409	\$ 95,089,409	\$ 141,965,598	21.46%	\$ 31,618,256	\$ 31,618,256	\$526,155,758
2011	\$ 664,266,863	\$ 47,075,413	7.09%	\$ 1,444,148,449	\$ -	\$ 1,444,148,449	\$ 101,903,246	\$ 101,903,246	\$ 149,978,659	22.43%	\$ 35,378,018	\$ 35,378,018	\$636,459,479
2012	\$ 667,089,997	\$ 47,275,483	7.09%	\$ 1,542,840,561	\$ -	\$ 1,542,840,561	\$ 108,867,244	\$ 108,867,244	\$ 156,142,727	23.41%	\$ 39,556,129	\$ 39,556,129	\$748,442,208
2013	\$ 669,925,129	\$ 47,476,404	7.09%	\$ 1,643,358,556	\$ -	\$ 1,643,358,556	\$ 115,960,081	\$ 115,960,081	\$ 163,436,485	24.40%	\$ 44,072,022	\$ 44,072,022	\$861,868,465
2014	\$ 672,772,311	\$ 47,678,179	7.09%	\$ 1,745,465,095	\$ -	\$ 1,745,465,095	\$ 123,165,010	\$ 123,165,010	\$ 170,843,189	25.39%	\$ 49,049,816	\$ 49,049,816	\$976,360,719
2015	\$ 675,631,593	\$ 47,880,811	7.09%	\$ 1,848,780,814	\$ -	\$ 1,848,780,814	\$ 130,455,263	\$ 130,455,263	\$ 178,336,074	26.40%	\$ 54,435,117	\$ 54,435,117	\$1,091,574,661

Funding Assumption: Pre-funding, Annual Employer Contributions Are Assumed to Equal ARC

Fiscal Year	Payroll Mid-Year	Normal Cost Mid-Year	NC as a % of Payroll	AAL	AVA	UAAAL	Amortization of UAAAL	Decreasing 30-year	Annual Required Contribution	ARC as a % of Payroll	BPs	Employer Contributions	Net OPEB Obligation
2006	\$ 650,329,396	\$ 46,087,689	7.09%	\$ 978,320,552	\$ -	\$ 978,320,552	\$ 69,033,097	\$ 69,033,097	\$ 115,120,786	17.70%	\$ 16,772,697	\$ 115,120,786	\$0
2007	\$ 653,093,296	\$ 46,283,562	7.09%	\$ 1,067,201,417	\$ 101,255,555	\$ 965,945,862	\$ 69,033,097	\$ 69,033,097	\$ 115,316,659	17.66%	\$ 19,638,052	\$ 115,316,659	\$0
2008	\$ 655,868,943	\$ 46,480,267	7.09%	\$ 1,158,666,734	\$ 205,838,043	\$ 952,828,690	\$ 69,033,097	\$ 69,033,097	\$ 115,513,364	17.61%	\$ 23,060,427	\$ 115,513,364	\$0
2009	\$ 658,656,366	\$ 46,677,808	7.09%	\$ 1,252,298,939	\$ 313,374,450	\$ 938,924,488	\$ 69,033,097	\$ 69,033,097	\$ 115,710,905	17.57%	\$ 27,108,819	\$ 115,710,905	\$0
2010	\$ 661,455,676	\$ 46,876,189	7.09%	\$ 1,347,584,382	\$ 423,398,348	\$ 924,186,034	\$ 69,033,097	\$ 69,033,097	\$ 115,909,286	17.52%	\$ 31,618,256	\$ 115,909,286	\$0
2011	\$ 664,266,863	\$ 47,075,413	7.09%	\$ 1,444,148,449	\$ 535,585,176	\$ 908,563,273	\$ 69,033,097	\$ 69,033,097	\$ 116,108,510	17.48%	\$ 35,378,018	\$ 116,108,510	\$0
2012	\$ 667,089,997	\$ 47,275,483	7.09%	\$ 1,542,840,561	\$ 650,837,415	\$ 892,003,146	\$ 69,033,097	\$ 69,033,097	\$ 116,308,580	17.44%	\$ 39,556,129	\$ 116,308,580	\$0
2013	\$ 669,925,129	\$ 47,476,404	7.09%	\$ 1,643,358,556	\$ 768,909,145	\$ 874,449,411	\$ 69,033,097	\$ 69,033,097	\$ 116,509,501	17.39%	\$ 44,072,022	\$ 116,509,501	\$0
2014	\$ 672,772,311	\$ 47,678,179	7.09%	\$ 1,745,465,095	\$ 889,622,643	\$ 855,842,453	\$ 69,033,097	\$ 69,033,097	\$ 116,711,276	17.35%	\$ 49,049,816	\$ 116,711,276	\$0
2015	\$ 675,631,593	\$ 47,880,811	7.09%	\$ 1,848,780,814	\$ 1,012,661,738	\$ 836,119,076	\$ 69,033,097	\$ 69,033,097	\$ 116,913,908	17.30%	\$ 54,435,117	\$ 116,913,908	\$0

The above calculations are based on the plan design, actuarial assumptions and methods and data from the actuarial valuation completed for the fiscal year ending June 30, 2006. This worksheet is subject to the same Actuarial Certifications, Reliances and Distribution as contained in that report. In projecting future valuation results, it was assumed that all actuarial assumptions (including investment return on assets) would be met and there would be no plan design, actuarial assumption or method changes made in the future. The actuarial assumptions were used to project payments made to future retirees. The active covered workforce reflects that approximately 2.5% of the workforce will terminate each year and that the average entry age and service of the active population will remain constant. The active pay for each individual is assumed to increase 3% per year. If contributions are made in excess of the benefit payments, it is assumed these contributions would be made in the middle of the fiscal year.

NOTE THAT THE SAME ACTUARIAL ASSUMPTIONS WERE USED FOR BOTH PROJECTIONS. HOWEVER, IF AN IRREVOCABLE TRUST IS NOT ESTABLISHED, THE DISCOUNT RATE WOULD LIKELY BE LOWERED, RESULTING IN HIGHER LIABILITIES AND A HIGHER ANNUAL REQUIRED CONTRIBUTION THAN THOSE SHOWN.



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HR SERVICES

City of San Diego Estimated Projection of Retiree Medical Benefit Plan Valuation Results

Projected Payroll Growth: 3.00% Annual Decrease in Active Counts: 2.50%
Investment Rate of Return: 6.00% Amortization period: 15 years

Funding Assumption: No Pre-funding

Fiscal Year	Payroll Mid-Year	Normal Cost Mid-Year	NC as a % of Payroll	AAL	AVA	UAAL	Amortization of UAAL 15-year	Annual Required Contribution	ARC as a % of Payroll	Benefit Disbursements	Employer Contributions	Net OPEB Obligation
2006	\$ 650,329,396	\$ 46,087,689	7.09%	\$ 978,320,552	\$ -	\$ 978,320,552	\$ 97,838,196	\$ 143,925,885	22.13%	\$ 16,772,697	\$ 16,772,697	\$130,912,219
2007	\$ 653,093,296	\$ 46,283,562	7.09%	\$ 1,067,201,417	\$ -	\$ 1,067,201,417	\$ 106,726,841	\$ 153,010,403	23.43%	\$ 19,638,052	\$ 19,638,052	\$262,603,108
2008	\$ 655,868,943	\$ 46,480,267	7.09%	\$ 1,158,666,734	\$ -	\$ 1,158,666,734	\$ 115,873,946	\$ 162,354,213	24.75%	\$ 23,060,427	\$ 23,060,427	\$394,732,683
2009	\$ 658,656,386	\$ 46,677,808	7.09%	\$ 1,252,298,939	\$ -	\$ 1,252,298,939	\$ 125,237,755	\$ 171,915,563	26.10%	\$ 27,108,819	\$ 27,108,819	\$526,861,544
2010	\$ 661,455,676	\$ 46,876,189	7.09%	\$ 1,347,584,382	\$ -	\$ 1,347,584,382	\$ 134,766,897	\$ 181,643,086	27.45%	\$ 31,618,256	\$ 31,618,256	\$658,686,132
2011	\$ 664,266,863	\$ 47,075,413	7.09%	\$ 1,444,148,449	\$ -	\$ 1,444,148,449	\$ 144,423,910	\$ 191,499,323	28.83%	\$ 35,378,018	\$ 35,378,018	\$791,123,876
2012	\$ 667,089,997	\$ 47,275,483	7.09%	\$ 1,542,840,561	\$ -	\$ 1,542,840,561	\$ 154,293,740	\$ 201,569,223	30.22%	\$ 39,556,129	\$ 39,556,129	\$923,937,697
2013	\$ 669,925,129	\$ 47,476,404	7.09%	\$ 1,643,358,556	\$ -	\$ 1,643,358,556	\$ 164,346,171	\$ 211,822,575	31.62%	\$ 44,072,022	\$ 44,072,022	\$1,056,952,545
2014	\$ 672,772,311	\$ 47,678,179	7.09%	\$ 1,745,465,095	\$ -	\$ 1,745,465,095	\$ 174,557,466	\$ 222,235,645	33.03%	\$ 49,049,816	\$ 49,049,816	\$1,189,848,666
2015	\$ 675,631,593	\$ 47,880,811	7.09%	\$ 1,848,780,814	\$ -	\$ 1,848,780,814	\$ 184,889,686	\$ 232,770,497	34.45%	\$ 54,435,117	\$ 54,435,117	\$1,322,336,990

Funding Assumption: Pre-funding, Annual Employer Contributions Are Assumed to Equal ARC

Fiscal Year	Payroll Mid-Year	Normal Cost Mid-Year	NC as a % of Payroll	AAL	AVA	UAAL	Amortization of UAAL 15-year	Annual Required Contribution	ARC as a % of Payroll	BP's	Employer Contributions	Net OPEB Obligation
2006	\$ 650,329,396	\$ 46,087,689	7.09%	\$ 978,320,552	\$ -	\$ 978,320,552	\$ 97,838,196	\$ 143,925,885	22.13%	\$ 16,772,697	\$ 143,925,885	\$0
2007	\$ 653,093,296	\$ 46,283,562	7.09%	\$ 1,067,201,417	\$ 130,912,219	\$ 936,289,198	\$ 97,838,196	\$ 144,121,758	22.07%	\$ 19,638,052	\$ 144,121,758	\$0
2008	\$ 655,868,943	\$ 46,480,267	7.09%	\$ 1,158,666,734	\$ 266,930,772	\$ 891,735,961	\$ 97,838,196	\$ 144,318,463	22.00%	\$ 23,060,427	\$ 144,318,463	\$0
2009	\$ 658,656,386	\$ 46,677,808	7.09%	\$ 1,252,298,939	\$ 407,789,408	\$ 844,509,531	\$ 97,838,196	\$ 144,516,004	21.94%	\$ 27,108,819	\$ 144,516,004	\$0
2010	\$ 661,455,676	\$ 46,876,189	7.09%	\$ 1,347,584,382	\$ 553,134,867	\$ 794,449,515	\$ 97,838,196	\$ 144,714,385	21.88%	\$ 31,618,256	\$ 144,714,385	\$0
2011	\$ 664,266,863	\$ 47,075,413	7.09%	\$ 1,444,148,449	\$ 702,762,551	\$ 741,385,898	\$ 97,838,196	\$ 144,913,609	21.82%	\$ 35,378,018	\$ 144,913,609	\$0
2012	\$ 667,089,997	\$ 47,275,483	7.09%	\$ 1,542,840,561	\$ 857,702,097	\$ 685,138,464	\$ 97,838,196	\$ 145,113,679	21.75%	\$ 39,556,129	\$ 145,113,679	\$0
2013	\$ 669,925,129	\$ 47,476,404	7.09%	\$ 1,643,358,556	\$ 1,017,842,372	\$ 625,516,184	\$ 97,838,196	\$ 145,314,600	21.69%	\$ 44,072,022	\$ 145,314,600	\$0
2014	\$ 672,772,311	\$ 47,678,179	7.09%	\$ 1,745,465,095	\$ 1,183,148,528	\$ 562,316,567	\$ 97,838,196	\$ 145,516,375	21.63%	\$ 49,049,816	\$ 145,516,375	\$0
2015	\$ 675,631,593	\$ 47,880,811	7.09%	\$ 1,848,780,814	\$ 1,353,455,841	\$ 495,324,373	\$ 97,838,196	\$ 145,719,007	21.57%	\$ 54,435,117	\$ 145,719,007	\$0

The above calculations are based on the plan design, actuarial assumptions and methods and data from the actuarial valuation completed for the fiscal year ending June 30, 2006. This worksheet is subject to the same Actuarial Certifications, Reliances and Distribution as contained in that report. In projecting future valuation results, it was assumed that all actuarial assumptions (including investment return on assets) would be met and there would be no plan design, actuarial assumption or method changes made in the future. The actuarial assumptions were used to project payments made to future retirees. The active covered workforce reflects that approximately 2.5% of the workforce will terminate each year and that the average entry age and service of the active population will remain constant. The active pay for each individual is assumed to increase 3% per year. If contributions are made in excess of the benefit payments, it is assumed these contributions would be made in the middle of the fiscal year.

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